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UNCLAS SECTION 01 OF 04 DUSHANBE 000475

SENSITIVE  
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COMMERCE FOR DAUSTR LILIENTFELD  
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SUBJECT: TAJIKISTAN SCENESETTER FOR DAUSTR CLAUDIO LILIENTFELD'S APRIL  
21-22 VISIT

REF: DUSHANBE 458

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¶1. (SBU) Embassy Dushanbe welcomes the upcoming visit of Deputy  
Assistant United States Trade Representative Claudio Lilienfeld.  
Following is an overview of key economic and trade issues in  
Tajikistan.

#### Overview

¶2. (SBU) The poorest former Soviet republic, Tajikistan is  
critically important to our efforts to stabilize Afghanistan and  
the region. The country faces serious challenges, however: the  
legacy of its civil war, poverty, isolation, massive labor  
migration, corruption, lack of government capacity, poor  
infrastructure, and low levels of investment, to name just a  
few. Furthermore, the global financial crisis has hit the  
country hard, resulting in a devalued national currency,  
declining remittances from Tajiks working abroad, and lower  
prices for Tajikistan's main exports, aluminum and cotton.

#### Economic Snapshot

¶3. (SBU) U.S. trade with Tajikistan remains minimal, due to  
several factors: the small size of the Tajik market, its  
distance from seaports and the United States, a general lack of  
transparency in business affairs, and government corruption and  
inefficiency. Despite this, Tajikistan has economic potential  
in a number of areas. On the production side, it possesses a  
wealth of relatively unexploited mineral deposits, a sizeable  
agricultural sector, and hydrocarbon resources, particularly gas  
and coal. On the market side, due precisely to the difficulties  
noted above, few firms are actively engaged in selling western  
products here. Despite Tajikistan's poverty, there is a real  
demand for such products. For Tajikistan to develop as an  
active trading partner for the United States and other  
countries, however, significant strides must be taken to ensure  
a more transparent business climate.

¶4. (SBU) Tajikistan's top leaders view foreign investment  
through the prism of their Soviet experience, and tend to favor  
large state-led investment projects. While acknowledging the  
need to attract private investment, the government has done  
little to stem the corruption and bureaucratic barriers that  
make Tajikistan an inhospitable environment for business. To  
some extent the government has not confronted these problems

since it has been able to attract state-led investment from China, Iran, and Russia, among others, to develop its road and energy infrastructure, while leaving much of the population to survive on remittances from Tajiks working in Russia. With the contraction of foreign investment as a result of the global financial crisis and the decline of the Russian economy, however, this may change.

15. (SBU) Tajikistan's largest industry is aluminum production, represented by a single firm, the Tajik Aluminum Company (Talco). Although it is state-owned, its profits flow to an offshore company said to be controlled by high-level Tajik government leaders. The state budget thus sees little of Talco's revenue. Steep declines in world aluminum prices since last July have even further reduced government income. Similar declines in world cotton prices have harmed Tajikistan's other main export sector. Government efforts to diversify agriculture have so far largely been rhetorical: farmers are still forced to grow cotton, and the government continues to support the sector with risky loans. According to media reports, only one-third of the \$41 million in loans made in 2008 have been repaid, and investors are seeking to restructure their debt. The government nevertheless intends to make almost \$50 million available this year to cotton sector investors. Many of these investors are politically connected.

16. (SBU) With few business opportunities in Tajikistan and deteriorating education and public services, much of the population relies on remittances from Tajiks abroad. Remittances in 2008 equaled over half of GDP -- the highest ratio in the world. In recent years, a million or more Tajiks (out of a total population of less than 7 million) went to work abroad, mostly in Russia. Migrant numbers had been increasing before the onset of the global recession, including boys of ever younger ages and, for the first time, significant numbers of women. Now, as a result of the global financial crisis, remittances have declined dramatically for the first time in six

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years. At the same time, returning unemployed migrant workers strain domestic services, already reduced due to lower-than-anticipated budget revenue.

17. (SBU) Tajikistan depends on its neighbors for the vast majority of its basic commodities. The situation became particularly dire in winter 2007-08, when brutal cold destroyed crops, seed stocks, fuel supplies, and livestock, making it more difficult for the rural poor to produce or afford food. Summer drought and locusts compounded the problem. The USG provided \$3.5 million in emergency assistance and delivered \$10.7 million in relief supplies donated by private firms. While this year's winter was much milder, the financial crisis means that many Tajiks face serious difficulties making ends meet. The USG has distributed \$6.3 million in emergency assistance this winter, and will deliver \$13 million of privately donated medical supplies in 2009. Unfortunately, our multi-year \$8.5 million Food-for-Peace program is ending, however, in part due to strong DOD support, we secured a one-time \$5.8 million Food-for-Peace-funded food delivery for this spring.

18. (SBU) Efforts to provide financial assistance to the government of Tajikistan have been hampered by a lack of transparency. The most notorious recent example was the National Bank of Tajikistan's (NBT) admission in December of 2007 that it had misreported its balance sheet to the IMF. As a condition for future assistance, the IMF required the NBT to immediately repay \$47 million in loans and submit to an audit. The key findings of this audit, by Ernst & Young, have just been released. While acknowledging some improvements, including the appointment of a new chairman of the bank, the audit describes a number of alarming problems, including inaccurate accounting, a lack of controls, and even efforts to mislead the auditors. It also reveals fundamental flaws in how the cotton industry is financed, and suggests that the bank cease direct lending to cotton financiers.

## Key Goals for Your Visit

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¶9. (SBU) Your visit supports a number of our policy goals by:

-- Expressing our interest in adding substance to the Trade and Investment Framework Agreement (TIFA) and working to ensure that it is mutually beneficial. Note that Washington intends to host.

-- Urging that political interference in the business affairs of U.S. firm Comsup Commodities and in the Grace Sun Min Church property dispute cease.

-- Encouraging the government to simplify and reform customs procedures.

-- Urging reform of the tax system, including reducing the number of taxes and the frequency of tax payments.

## Background

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¶10. (SBU) Last year's TIFA action plan, developed during September meetings in Dushanbe, focused on improving investment, overcoming practical barriers, creating a single-window business registration process, and improving access to business information. So far, little concrete progress has been made in any of these areas. Investment has not noticeably increased, both as a result of the crisis but also because impediments have not been removed. While work has been done on the single-window system, no concrete steps have been made. See reftel for more on post's thoughts about where we may go with TIFA.

¶11. (SBU) At the moment the only U.S. firm with significant investment interests in Tajikistan is the mining firm Comsup Commodities. Comsup's experience may be more of a cautionary tale than a positive example for other potential investors. In 2004 Comsup opened a joint venture with the Tajik Ministry of Industry to mine antimony; two years later, at the Ministry's request, Comsup bought out the Ministry and became the sole owner of the operation. At about the same time, Kholnazar Kholiqov, the former director of a mine subsequently bought by Comsup, began pressuring Comsup to sell its production at below-market prices to his new company, Salosa, LLC, which would then serve as a middleman in selling antimony overseas. Salosa has received powerful support from the Prime Minister's office,

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which has insisted that Comsup sell to Salosa. A Comsup representative recently took the issue up with Matlubkhon Davlatov, President Rahmon's Advisor on Economic Policy, explaining that Comsup will not make further investments in Tajikistan unless the political pressure stops and other problems are resolved. He noted that international financial institutions such as the EBRD and ADB -- the only viable sources of finance for further investments -- wouldn't touch a project that is receiving such political interference. Davlatov suggested that Comsup draft a letter outlining the difficulties and send it directly to the President. Comsup is hesitant to take this step, however, fearing unpredictable results. Indeed, the process of farming out the Presidential letter to various parts of the Tajik government for action could actually delay resolution of Comsup's problems.

¶12. (SBU) Tajikistan's customs procedures are byzantine, time-consuming, and, quite frequently, corrupt. Reform of the system is essential to attract more commerce. Among other reforms, customs automation should be improved, including the establishment of a single declaration processing system, a single administrative document for import and export, and a one-stop-shop for processing. USAID is supporting the Regional Trade Liberalization and Customs Program, which assists in the automation process and works with the government on preparing for WTO accession. In the future, we are looking to improve the transit system, including establishing bonded warehousing.

¶13. (SBU) Another essential area of reform is the tax system. There are currently seventeen different kinds of taxes affecting all kinds of business activity. Not only is the system complicated, but the different taxes do not effectively complement one another. A local businessman told us earlier this year that if a business wanted to work entirely openly in Tajikistan, it would have to pay as much as 87% of its income in taxes. To improve its business environment, the government should reduce the number of individual taxes and the frequency of required tax payments. This will ease the administrative burden on businesses and increase tax revenue for the government. The government should adopt policies to make the Free Economic Zones a reality by rationalizing the registration process and specifying the preferential conditions for business in these zones. USAID has been assisting Tajikistan through its Business Environment Improvement Project, the main goal of which is to improve the country's World Bank "Doing Business" scores, on criteria such as ease of starting and ending a business, paying taxes, getting construction permits, hiring staff, etc. Tajikistan ranks near the bottom of the list.

¶14. (SBU) A major impediments to doing business in Tajikistan is a lack of transparency on property issues. Government officials use outmoded property codes and a corrupt civil court system to deprive many of their rights. City of Dushanbe officials -- under the direct orders of the Mayor -- have been frequent practitioners. One example is the Grace Sun Min Mission Center, a church with ties to the U.S. and Korea, which purchased property in 1999 and invested an estimated \$500,000 in renovating the buildings on the lot. City officials have been trying since 2004 to take the property back by filing legal actions, but Tajikistan's economic courts consistently ruled in favor of the Mission Center. That changed in 2008, however, when the Supreme Economic Court determined that the Mission Center must hand over its property to the city, reasoning that the city itself never properly privatized the land in the first place. The Court also ruled that the city must compensate the Mission Center only for the original 1999 purchase price of just over \$5,000. Observers of the proceedings have noted numerous irregularities, and have concluded that city officials have manipulated the economic courts in order to obtain a favorable judgment. The government has been employing this same strategy against other entities that hold property in prime locations throughout the city, including a popular market near the embassy, a successful gas distribution company, and an international organization.

¶15. (SBU) Comment: While the world financial crisis has serious consequences for Tajikistan, it could nevertheless ultimately yield some positive results. In particular, it may provide some incentives for the authorities to confront longstanding impediments to local business development and foreign investment. It is already resulting in increased transparency in order to attract loans and other budget support from the IMF and World Bank. The question is whether this tendency will be

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strengthened and supported to the extent that it improves the trade and investment climate in Tajikistan. End comment.  
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